

### III. *Puerto Rico and the Oversight Board's Authority*

#### A. Introduction

In the late 2000s, the Commonwealth of Puerto Rico experienced a severe economic decline.<sup>1</sup> At the same time, it issued a large amount of municipal bonds to pay for its health care, infrastructure, and various social programs.<sup>2</sup> Puerto Rico's government has operated at a deficit every year since 2002.<sup>3</sup> Rather than reducing its deficit by cutting spending or raising taxes, Puerto Rico's government has issued debt to finance its operations.<sup>4</sup> "The level of outstanding public debt expressed as a percentage of annual GNP rose from about sixty percent in 2000 to more than 100 percent in 2013."<sup>5</sup> Debt ratios at this level are a significant impediment to economic growth.<sup>6</sup> By comparison, the European Union Stability and Growth Pact states that all countries in the Eurozone should aim to keep their total public debt below sixty percent of Gross Domestic Product (GDP).<sup>7</sup> If a country breaks the sixty percent level, it must take measures to reduce the

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<sup>1</sup> U.S. DEP'T OF THE TREASURY, PUERTO RICO'S ECONOMIC AND FISCAL CRISIS, [https://www.treasury.gov/connect/blog/Documents/Puerto\\_Ricos\\_fiscal\\_challenges.pdf](https://www.treasury.gov/connect/blog/Documents/Puerto_Ricos_fiscal_challenges.pdf) [<http://perma.cc/5569-X3BZ>] ("[S]ince . . . 2006 [Puerto Rico's] economy has shrunk by more 10 percent and employment on the island has fallen by 14 percent.").

<sup>2</sup> U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-18-160, U.S. TERRITORIES PUBLIC DEBT OUTLOOK (2017) ("Between fiscal years 2005 and 2014 . . . Puerto Rico's total public debt outstanding (public debt) grew from \$39.2 billion to \$67.8 billion, reaching 66 percent of Gross Domestic Product.").

<sup>3</sup> U.S. GOV'T ACCOUNTABILITY OFFICE., GAO-18-387, PUERTO RICO FACTORS CONTRIBUTING TO THE DEBT CRISIS AND POTENTIAL FEDERAL ACTIONS TO ADDRESS THEM (2018).

<sup>4</sup> *Id.*

<sup>5</sup> FED. RESERVE BANK OF N.Y., AN UPDATE ON THE COMPETITIVENESS OF PUERTO RICO'S ECONOMY (July 31, 2014), <https://www.newyorkfed.org/medialibrary/media/outreach-and-education/puerto-rico/2014/Puerto-Rico-Report-2014.pdf> [<https://perma.cc/9UQM-HURG>].

<sup>6</sup> *See id.*

<sup>7</sup> European Parliament Briefing, Stability and Growth Pact—An Overview of the Rules (Dec. 18, 2015), [http://www.europarl.europa.eu/RegData/etudes/note/join/2014/528745/IPOL-ECON\\_NT\(2014\)528745\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/note/join/2014/528745/IPOL-ECON_NT(2014)528745_EN.pdf) [<http://perma.cc/4HAK-TQBK>] (reporting that for countries whose debt is higher than sixty percent of GDP, compliance with the debt reduction benchmark is part of the medium-term objective).

deficits or face fines up to 0.5% of GDP.<sup>8</sup> A fiscal plan released by the Government of Puerto Rico listed total public debt outstanding at \$74.3 billion as of February 2017.<sup>9</sup> Between August 2015 and May 2018, Puerto Rico defaulted on over \$1.5 billion in debt.<sup>10</sup>

I will first review in Section B Puerto Rico's response to the economic decline and the litigation that resulted. In this context I discuss Congress's enactment of the Puerto Rico Oversight, Management, and Economic Stability Act which created the Financial Oversight and Management Board. Further, I will discuss the disagreement between the Financial Oversight and Management Board and the Governor of Puerto Rico over the former's authority. In Section C I will examine how Puerto Rico's unique status as a U.S. Territory impacts the disagreement and how the uniformity requirement of the Bankruptcy Clause of the Constitution affects the litigation. Section D concludes with an examination of how Hurricane Maria, which significantly damaged Puerto Rico in 2017, might result in a more pragmatic approach going forward.

## **B. The Recovery Act and PROMESA**

In 2014, Puerto Rico enacted the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (Recovery Act).<sup>11</sup> This allowed financially distressed Puerto Rican public corporations to restructure their debt obligations.<sup>12</sup> The Recovery Act's purpose was to balance the interest of creditors and stakeholders with the interest of Puerto Rico in protecting its citizens by continuing to provide essential government services.<sup>13</sup> Significantly, the Recovery Act did not stabilize the capital markets.<sup>14</sup> In response, rating agencies downgraded

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<sup>8</sup> *Id.* at 5 (identifying the possible sanctions that govern the excessive deficit procedure).

<sup>9</sup> U.S. GOV'T ACCOUNTABILITY OFFICE., *supra* note 2, at 13 (stating total public debt outstanding of \$74.3 billion as of February 2017).

<sup>10</sup> U.S. GOV'T ACCOUNTABILITY OFFICE., *supra* note 3.

<sup>11</sup> 2014 P.R. Laws Act No. 71. *See* Restructuring Alert from Orrick, Herrington & Sutcliffe LLP, Lorraine McGowen et al., Summary of Puerto Rico Public Corporation Debt Enforcement & Recovery Act (July 2014).

<sup>12</sup> Restructuring Alert, *supra* note 11, at 1.

<sup>13</sup> *Id.*

<sup>14</sup> *Id.* at 10 ("If the goal . . . was to stabilize the capital market and insulate the Commonwealth of Puerto Rico's general obligation and COFINA bonds from the financial distress of the Commonwealth's other public corporations, that goal has failed.").

securities issued by Puerto Rico because the Recovery Act made restructuring or default more likely.<sup>15</sup> However, in 2015 a United States District Court struck down the Recovery Act as being preempted by the U.S. Bankruptcy Code.<sup>16</sup> The court ruled that section 903(1) of the U.S. Bankruptcy Code preempted the Recovery Act.<sup>17</sup> This was later affirmed by the Supreme Court.<sup>18</sup>

As a result of these cases, in June 2016 Congress enacted the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA).<sup>19</sup> Title I of PROMESA established a Financial Oversight and Management Board (Oversight Board),<sup>20</sup> the purpose of which is to provide a method for a covered territory to achieve fiscal responsibility and access to the capital markets.<sup>21</sup> The Oversight Board consists of seven voting members appointed by the President, as well as the Governor of Puerto Rico or the Governor's designee, as a non-voting member.<sup>22</sup> PROMESA gives the Oversight Board broad powers to hold hearings, take testimony, and receive evidence, accept, use, and dispose of gifts, bequests, or devises of services or property, both real and person, for aiding or facilitating the work of the Oversight Board, issue subpoenas, enter into contracts, and investigate disclosure and selling practices of bonds.<sup>23</sup> Further, neither the Governor nor the

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<sup>15</sup> *Id.*

<sup>16</sup> *Franklin Cal. Tax-Free Tr. v. Puerto Rico*, 85 F. Supp. 3d 577, 583 (2015) (“Because the Recovery Act is preempted by the federal Bankruptcy Code, it is void pursuant to the Supremacy Clause of the United States Constitution.”).

<sup>17</sup> *See* 11 U.S.C. § 903(1) (2012) (reserving State power to control municipalities); 11 U.S.C. § 101(52) (2012) (excluding Puerto Rico as a debtor under Chapter 9); 85 F. Supp. 3d. at 601 (“Section 903(1)’s text and legislative history provide direct evidence of Congress’s clear and manifest purpose to preempt state laws that prescribe a method of composition of municipal indebtedness that binds nonconsenting creditors . . . and to include Puerto Rico laws in this preempted arena . . .”).

<sup>18</sup> *Puerto Rico v. Franklin Cal. Tax-Free Tr.*, 136 S. Ct. 1938, 1949 (2016) (holding federal law preempts the Recovery Act).

<sup>19</sup> Pub. L. No. 114-187, 130 Stat. 549 (2016) (to be codified at 48 U.S.C. §§ 2101–2241).

<sup>20</sup> *Id.* § 101, 130 Stat. at 553 (“A Financial Oversight and Management Board is hereby established for Puerto Rico.”).

<sup>21</sup> *Id.* (identifying the purpose of the Oversight Board as providing a method for a territory to fiscal responsibility and access to the capital markets).

<sup>22</sup> *Id.* § 101, 130 Stat. at 554–56 (“The Oversight Board shall consist of seven members.”).

<sup>23</sup> *Id.* (listing the powers of the Oversight Board).

Legislature may exercise any control or supervision over the Oversight Board or enact any statute, policy, or rule that would impair the purposes of PROMESA, as determined by the Oversight Board.<sup>24</sup>

Title III of PROMESA consists of a court-supervised debt restructuring procedure.<sup>25</sup> For cases in which the debtor is a territory, the Chief Justice of the United States Supreme Court designates “a district court judge to sit by designation to conduct the case.”<sup>26</sup> On May 2, 2017, Governor Nevares sent a letter to the chairman of the Oversight Board stating the government of Puerto Rico’s desire to make a plan to readjust its debt under Title III of PROMESA.<sup>27</sup> Governor Nevares stated that the good-faith effort Puerto Rico made to reach a restructuring agreement with its creditors was not sufficient to achieve the Fiscal Plan as set forth by the Oversight Board earlier that year.<sup>28</sup> Therefore, the next best step for Puerto Rico was to enter into Title III to adjust its debt to a workable level.<sup>29</sup> As of May 3, 2017, Puerto Rico’s debt equaled approximately \$74 billion of bond debt and \$49 billion of unfunded pension liabilities.<sup>30</sup> Chief Justice Roberts then picked federal court Judge Laura Taylor Swain to preside over the case seeking bankruptcy-like relief under Title III.<sup>31</sup>

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<sup>24</sup> *Id.* § 108, 130 Stat. at 563 (stating that neither the Governor nor the Legislature may exercise control or supervision over the Oversight Board or enact or enforce any statute, resolution, or policy that would impair the purposes of PROMESA).

<sup>25</sup> *Id.* § 301, 130 Stat. at 577 (setting forth the adjustment of debts subchapter).

<sup>26</sup> *Id.* § 308, 130 Stat. at 582 (“For cases in which the debtor is a territory, the Chief Justice of the United States shall designate a district court judge to sit by designation to conduct the case.”).

<sup>27</sup> Letter from Governor Ricardo Rosselló Nevares, P.R., to José Carrión, Chairman, Fin. Oversight & Mgmt. Bd. (May 2, 2017) (“I am hereby making this submission to the Financial Oversight and Management Board for Puerto Rico . . . as appointed under [PROMESA] . . . representing that as of the date hereof the Government of Puerto Rico . . . desires to effect a plan to adjust its debt under Title III of PROMESA.”).

<sup>28</sup> *See id.*

<sup>29</sup> *See id.*

<sup>30</sup> KOBRE & KIM LLP, THE FINANCIAL OVERSIGHT & MANAGEMENT BOARD FOR PUERTO RICO SPECIAL INVESTIGATION COMMITTEE INDEPENDENT INVESTIGATOR’S FINAL INVESTIGATIVE REPORT 2 (2018).

<sup>31</sup> Matthew Goldstein, *Judge in Puerto Rico’s Debt Lawsuit Handled Major Financial Cases*, N.Y. Times (May 5, 2017), <https://www.nytimes.com/2017/05/05/business/dealbook/judge-puerto-rico-case.html>.

In April 2018, the Oversight Board issued its New Fiscal Plan for Puerto Rico (New Fiscal Plan).<sup>32</sup> The New Fiscal Plan outlined several policy and structural initiatives.<sup>33</sup> However, Governor Nevares rejected the Oversight Board's plan for cutting pension benefits as well as several other initiatives he viewed as public policy issues.<sup>34</sup> As a result, the Oversight Board issued a notice of violation under PROMESA section 202(c)(1)(B)(i) to Governor Nevares.<sup>35</sup> After a period of negotiations, the Oversight Board and Governor Nevares went to court to determine whether the challenged initiatives were non-binding recommendations by the Oversight Board or rather mandatory provisions that can be enforced.<sup>36</sup>

The Oversight Board argued that PROMESA section 108(a) prohibits the Commonwealth government from taking any act contrary to those purposes, "as determined by the Oversight Board."<sup>37</sup> The Oversight Board also argued that PROMESA section 4 preempts any Commonwealth law "inconsistent" with it.<sup>38</sup> Governor Nevares argued that because section 205 of PROMESA authorizes the Oversight Board to make recommendations to ensure compliance with the Fiscal Plan and to improve Commonwealth governance, the Commonwealth is free to reject or treat as optional anything Plaintiffs describe as a "recommendation" or "policy initiative."<sup>39</sup> Specifically, Governor Nevares identified five Oversight Board measures included in the New Fiscal Plan that he had rejected: (i) private-sector human-capital and labor reforms; (ii) pension reforms; (iii) government agency consolidations; (iv) compensation related initiatives; and (v) reductions in appropriations to the University of Puerto Rico.<sup>40</sup> The Governor argued that the Oversight Board lacked the power to impose these

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<sup>32</sup> See generally FIN. OVERSIGHT & MGMT. BD. FOR P.R., NEW FISCAL PLAN FOR PUERTO RICO: RESTORING GROWTH AND PROSPERITY (2018).

<sup>33</sup> *Id.*

<sup>34</sup> Michelle Kaske et al., *Puerto Rico Board Backs Fiscal Plan amid Clash with Governor*, BLOOMBERG (Apr. 19, 2018, 5:12 PM), <https://www.bloomberg.com/news/articles/2018-04-19/puerto-rico-board-passes-fiscal-plan-amid-clash-with-governor>.

<sup>35</sup> *Nevares v. Fin. Oversight & Mgmt. Bd. (In re Fin. Oversight & Mgmt. Bd.)*, 330 F. Supp. 3d 685 (D.P.R. 2018).

<sup>36</sup> *Id.* at 693.

<sup>37</sup> *Id.* at 700.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 690.

<sup>40</sup> *Id.* at 691–93 (outlining the five measures in the Oversight Board's Fiscal Plan that the Governor had rejected).

measure on the Government of Puerto Rico.<sup>41</sup> The case ultimately determined whether the Oversight Board could, through fiscal plans and budgets, mandate actions implementing policies that have specifically been rejected by the Governor, and whether the Oversight Board's budget can modify or override pre-PROMESA Puerto Rico law.<sup>42</sup>

The two controversial sections of PROMESA were 205 and 201.<sup>43</sup> Section 205 of PROMESA authorizes the Oversight Board to "submit recommendations" to the Governor or the Legislature of Puerto Rico at any time "on actions the territorial government may take to ensure compliance with the Fiscal Plan, or to otherwise promote the financial stability, economic growth, management responsibility, and service delivery efficiency of" the Government.<sup>44</sup> If the Government of Puerto Rico declines to adopt a recommendation, the Governor or Legislature must include in the statement "explanations for the rejection of the recommendations," and the statement must be submitted to the President and Congress of the United States as well as to the Oversight Board.<sup>45</sup> Section 205 does not further address what happens to rejected recommendations.<sup>46</sup> Section 201(b)(1)(K) provides that a fiscal plan shall "adopt appropriate recommendations submitted by the Oversight Board under Section 205."<sup>47</sup> Section 201(d)(2) states that "if the Governor fails to submit to the Oversight Board a Fiscal Plan that the Oversight Board determines in its sole discretion satisfies the requirement set forth in subsection (b) by the time specified . . . the Oversight Board shall develop and submit to the Governor and the Legislature a Fiscal Plan that satisfies the requirements set forth in subsection (b)."<sup>48</sup> Further, section 201(e)(2) states "if the Oversight

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<sup>41</sup> *Id.* at 690 ("The Governor asserted that the Oversight Board lacks power to impose these measures on the Government.").

<sup>42</sup> *Id.* at 698.

<sup>43</sup> *Id.* ("At the core of this dispute are questions of statutory interpretation regarding the interplay of Sections 205 and 201(b)(1)(K) of PROMESA . . .").

<sup>44</sup> Puerto Rico Oversight, Management, and Economic Stability Act, Pub. L. No. 114-187, § 205, 130 Stat. 573 (2016).

<sup>45</sup> *Id.* § 205, 130 Stat. at 574.

<sup>46</sup> *Id.* § 205, 130 Stat. at 573.

<sup>47</sup> *Id.* § 210, 130 Stat. at 564. *See also In re Fin. Oversight & Mgmt. Bd.*, 330 F. Supp. 3d at 699 ("Section 201(b)(1)(K) expressly provides that a fiscal plan shall 'adopt appropriate recommendations submitted by the Oversight Board under Section 205(a).').

<sup>48</sup> Pub. L. No. 114-187, § 201, 130 Stat. at 565.

Board develops a Fiscal Plan under subsection (d)(2), such Fiscal Plan shall be deemed approved by the Governor.”<sup>49</sup> Judge Swain held that the Oversight Board has the power to make binding policy choices, stating that “the power bestowed on the Oversight Board by § 201(b)(1)(K) of PROMESA allows the Oversight Board to make binding policy choices for the Commonwealth, notwithstanding the Governor’s rejection of section 205 recommendations.”<sup>50</sup> Judge Swain noted that the Oversight Board’s power is consistent with PROMESA’s framework in light of the Oversight Board’s mandate, sole discretion to certify fiscal plans and put budgets of its own into effect, and PROMESA’s preemption of laws inconsistent with its provisions.<sup>51</sup> Additionally, Judge Swain noted commentary in the legislative history of PROMESA was generally consistent with the view that certified fiscal plans would be able to adopt recommendations even absent approval by the Government.<sup>52</sup>

### C. Puerto Rico and the Uniformity Requirement of the Bankruptcy Clause

The issues surrounding the Oversight Board, Governor Nevares, and PROMESA are largely a result of the uncertainty of Puerto Rico’s legal status. As a U.S. territory, Puerto Rico is neither a sovereign government nor a municipality.<sup>53</sup> Congress might treat Puerto Rico in ways that would otherwise be prohibited if it were a state.<sup>54</sup> As it relates to bankruptcy, Puerto Rico issues debt as a municipality, yet has historically lacked recourse to municipal bankruptcy

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<sup>49</sup> *Id.*

<sup>50</sup> 330 F. Supp. 3d at 700.

<sup>51</sup> *Id.*

<sup>52</sup> *Id.* at 702 (recounting a statement of Senator Menendez indicating that the Oversight Board can incorporate or adopt their recommendations, even those not adopted by the Governor or Legislature).

<sup>53</sup> Stephen Kim Park & Tim R. Samples, *Puerto Rico’s Debt Dilemma and Pathways Toward Sovereign Solvency*, 54 AM. BUS. L.J. 9, 10 (2017) (“Puerto Rico is neither a sovereign government nor a municipality.”).

<sup>54</sup> See *Harris v. Rosario*, 446 U.S. 651, 651–62 (1980) (stating that Congress “may treat Puerto Rico differently from States so long as there is a rational basis for its actions”); Stephen J. Lubben, *Puerto Rico and the Bankruptcy Clause*, 88 AM. BANKR. L.J. 553, 556 (describing Puerto Rico as “in a kind of constitutional limbo.”).

under Chapter 9 of the U.S. Bankruptcy Code.<sup>55</sup> Puerto Rico was prohibited from restructuring debts through bankruptcy prior to PROMESA as Puerto Rico is specifically excluded from Chapter 9 of the U.S. Bankruptcy Code.<sup>56</sup> This has led to a variety of proposals to alleviate the debt problems: statehood for Puerto Rico, contractual negotiations, and allowing Puerto Rico's debt to be subject to Chapter 9 procedures have all been debated.<sup>57</sup> Further, the legal uncertainty of Puerto Rico persists in PROMESA's balance between the Oversight Board and the Government.<sup>58</sup>

The Constitution gives Congress the power to establish uniform laws on the subject of bankruptcy throughout the United States.<sup>59</sup> In his concurring opinion finding the Recovery Act preempted, Judge Torruella wrote that attempts to establish bankruptcy legislation that is not uniform with regards to the rest of the United States violates the uniformity requirement of the Bankruptcy Clause of the Constitution.<sup>60</sup> That is, prohibiting Puerto Rico from authorizing its municipalities to request Chapter 9 relief, while allowing all the states to benefit from such power, is not consistent with the uniformity requirement.<sup>61</sup> The Supreme Court has noted that the uniformity

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<sup>55</sup> Park & Samples, *supra* note 53, at 10 (“Puerto Rico issues debt as a municipality yet has historically lacked recourse to municipal bankruptcy under Chapter 9 of the U.S. Bankruptcy Code.”).

<sup>56</sup> 11 U.S.C. § 101(52) (2012) (excluding Puerto Rico as a debtor under Chapter 9); Park & Sample, *supra* note 53, at 29.

<sup>57</sup> Cory Howard, *Puerto Rico's Municipal Bond Dilemma: Is Statehood the Only Viable Option?* 83 REV. JUR. DIG. U.P.R. 15, 17 (2013); John A. E. Pottow, *What Bankruptcy Law Can and Cannot Do for Puerto Rico*, REV. JUR. U.P.R. 85, 689–704 (2016).

<sup>58</sup> *Nevares v. Fin. Oversight & Mgmt. Bd. (In re Fin. Oversight & Mgmt. Bd.)*, 330 F. Supp. 3d 685, 701 (D.P.R. 2018).

<sup>59</sup> U.S. CONST. art. I, § 8, cl. 4. (“The Congress shall have power . . . To establish . . . uniform laws on the subject of Bankruptcies throughout the United States . . .”).

<sup>60</sup> *Franklin Cal. Tax-Free Tr. v. Puerto Rico*, 805 F.3d 322, 346 (1st Cir. 2015) (Torruella, J., concurring) (remarking that attempts to establish bankruptcy legislation that is not uniform with regards to the rest of the United States violates the uniformity requirement of the Bankruptcy Clause of the Constitution).

<sup>61</sup> *Id.* (“The term ‘uniform’ is unequivocal and unambiguous language, which is defined as ‘always the same, as in character or degree; unvarying,’ and as ‘[c]haracterized by a lack of variation; identical or consistent.’ Prohibiting Puerto Rico from authorizing its municipalities to request Chapter 9 relief,



requirement prohibits Congress from enacting bankruptcy laws that specifically apply to the affairs of only one named regional debtor.<sup>62</sup> Therefore PROMESA is a bankruptcy law made for Puerto Rico alone.<sup>63</sup>

Despite the apparent non-uniform bankruptcy treatment of Puerto Rico, PROMESA would likely survive a constitutional challenge on uniformity grounds. The uniformity provision does not prevent Congress from taking into account differences that exist between different parts of the country, and to create legislation to resolve geographically isolated problems.<sup>64</sup> The Supreme Court has rejected the interpretation that the uniformity required by the Constitution is geographic.<sup>65</sup> Instead, there is flexibility inherent in the constitutional provision, and the uniformity clause requires bankruptcy laws apply equally to all creditors and debtors.<sup>66</sup> As long as it can be said to operate uniformly upon the creditors and debtors, PROMESA and the Oversight Board are likely a constitutional effort of Congress to deal with a geographically isolated problem.<sup>67</sup> It is unclear how much flexibility Congress has in such instances.<sup>68</sup> The apparent flexibility may be significant however, as a federal law has only been declared unconstitutional by the Supreme Court on uniformity grounds one time.<sup>69</sup>

#### D. Conclusion

On September 20, 2017, Hurricane Maria struck Puerto Rico, causing unprecedented damage.<sup>70</sup> Thousands of Puerto Rico citizens were left homeless and schools, hospitals, and businesses were

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while allowing all the states to benefit from such power, is hardly in keeping with these definitions.”).

<sup>62</sup> *Ry. Labor Execs.’ Ass’n v. Gibbons*, 455 U.S. 457, 473 (1982).

<sup>63</sup> Stephen J. Lubben, *PROMESA and the Bankruptcy Clause: A Reminder About Uniformity*, BROOK. J. CORP. FIN. & COM. L. (forthcoming) (manuscript at 22).

<sup>64</sup> *Reg’l Rail Reorganization Act Cases*, 419 U.S. 102, 159 (1974).

<sup>65</sup> *Id.* at 158.

<sup>66</sup> *See id.* at 158–60.

<sup>67</sup> Lubben, *supra* note 63, at 7.

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> FIN. OVERSIGHT & MGMT. BD. FOR P.R., *NEW FISCAL PLAN FOR PUERTO RICO: RESTORING GROWTH AND PROSPERITY* (2018).

destroyed.<sup>71</sup> In response to this, the Oversight Board formally requested the Governor submit a revised fiscal plan.<sup>72</sup> However, PROMESA and the Oversight Board were designed before Hurricane Maria.<sup>73</sup> This has resulted in calls for additional assistance for Puerto Rico.<sup>74</sup>

In July 2018, Senator Elizabeth Warren introduced the United States Territorial Relief Act of 2018 (U.S. Territorial Relief Act).<sup>75</sup> The U.S. Territorial Relief Act is designed to provide additional debt relief to Puerto Rico considering both the economic problems and impact from Hurricane Maria.<sup>76</sup> The U.S. Territorial Relief Act has three components.<sup>77</sup> First, Puerto Rico is given the option to terminate its public unsecured debt if two of three criteria are met.<sup>78</sup> The three criteria are a population decrease of five percent over ten years, receipt of major federal disaster assistance, and per capita debt exceeding \$15,000.<sup>79</sup> Puerto Rico's Governor and each body of its legislature must approve the debt relief.<sup>80</sup> Second, a special compensation fund is designated to allocate \$7.5 billion to eligible Puerto Rican creditors and \$7.5 billion to eligible mainland creditors.<sup>81</sup> Third, the U.S. Territorial Relief Act establishes a commission of experts from Puerto Rico is created to perform a comprehensive audit of the causes and sources of Puerto Rico's debt and issue periodic reports.<sup>82</sup> The U.S. Territorial Relief Act has received support from several prominent law

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<sup>71</sup> *Id.* (describing how basic utilities were completely shut down and took months become operational).

<sup>72</sup> *Id.*

<sup>73</sup> *See* Letter from Adam J. Levitin, Professor, Georgetown Univ. Law Ctr., to Senators Elizabeth Warren and Bernie Sanders (July 25, 2018).

<sup>74</sup> *See id.*

<sup>75</sup> United States Territorial Relief Act of 2018, S. 3262, 115th Cong. (2018) (introducing the bill which was referred to the committee on Energy and Natural Resources).

<sup>76</sup> *Id.*

<sup>77</sup> *See id.*

<sup>78</sup> *Id.* § 102.

<sup>79</sup> *Id.* at § 2.

<sup>80</sup> *Id.* § 307.

<sup>81</sup> *Id.* § 205 (describing the Puerto Rico Debt Restructuring Compensation Fund).

<sup>82</sup> *Id.* § 302–03.

professors.<sup>83</sup> After it was introduced to the Senate, the U.S. Territorial Relief Act was referred to the Committee on Energy and Natural Resources on July 25, 2018.<sup>84</sup> The bill has yet to progress out of the Committee.<sup>85</sup> However, a related bill sponsored by Representative Nydia Velazquez was introduced in the House on September 13, 2018.<sup>86</sup> On September 24, the related House bill was referred to the Natural Resources Subcommittee on Indian, Insular, and Alaska Native Affairs, where it remains.<sup>87</sup>

Regardless of whether the U.S. Territorial Relief Act is embraced, the Oversight Board will likely need to reevaluate its approach toward achieving fiscal responsibility and access to the capital markets for Puerto Rico after Hurricane Maria. This will likely manifest in a more pragmatic approach as it relates to public policy issues that the Oversight Board and Governor Nevares have conflicted over previously. Even though several sections of PROMESA are adopted from the Bankruptcy code, there are substantial differences that present novel challenges for Puerto Rico. Ultimately, providing debt relief and helping Puerto Rico gain access to the capital markets after Hurricane Maria will require close collaboration between the Government of Puerto Rico and the Oversight Board.

Joseph Markel<sup>88</sup>

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<sup>83</sup> See Letter from Adam J. Levitin, *supra* note 74; Letter from Laurence H. Tribe, Professor, Harvard Univ., to Senators Elizabeth Warren and Bernie Sanders (July 25, 2018).

<sup>84</sup> S.3262 - United States Territorial Relief Act of 2018, CONGRESS.GOV, <https://www.congress.gov/bill/115th-congress/senate-bill/3262/all-actions> [<https://perma.cc/KJM8-XNB2>].

<sup>85</sup> *Id.*

<sup>86</sup> United States Territorial Relief Act of 2018, H.R. 6827, 115th Cong. (2018); H.R.6827 - United States Territorial Relief Act of 2018, CONGRESS.GOV, <https://www.congress.gov/bill/115th-congress/house-bill/6827/all-actions> [<https://perma.cc/7Y4X-RQC3>]

<sup>87</sup> *Id.*

<sup>88</sup> Student, Boston University School of Law (J.D. 2020).

#### ***IV. Executive Influence on the Federal Reserve***

##### **A. Introduction**

On July 20, 2018 President Donald Trump tweeted from his personal Twitter account, “The United States should not be penalized because we are doing so well. Tightening now hurts all that we have done. The U.S. should be allowed to recapture what was lost due to illegal currency manipulation and BAD Trade Deals. Debt coming due & we are raising rates - Really?”<sup>1</sup> The tweet came in the wake of a historically unprecedented interview with CNBC in which President Trump voiced his displeasure with the Federal Reserve (Fed) for raising interest rates twice in 2018, with signs pointing to further rate hikes by the end of the year.<sup>2</sup> In the interview the President told CNBC’s Joe Kernen, “I’m not thrilled . . . [b]ecause we go up and every time you go up they want to raise rates again. I don’t really—I am not happy about it. But at the same time I’m letting them do what they feel is best.”<sup>3</sup> Following his remarks, the White House issued a statement reiterating that the President respects the Fed’s independence and was simply vocalizing his known personal views on interest rates.<sup>4</sup>

President Trump’s comments sparked concern amongst economists, as they represent the first time a President publically criticized the Fed Chairman (Chairman) since President H.W. Bush told the New York Times he wanted then Chairman Alan Greenspan to lower interest rates.<sup>5</sup> Concerns of history repeating itself also stem from a long period of inflation and low economic growth in the 1970s and 80s, known as “stagflation” which followed the decision by then-

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<sup>1</sup> Donald J. Trump (@realDonaldTrump), TWITTER (July 20, 2018, 9:51 AM), <https://twitter.com/realDonaldTrump/status/1020290163933630464> [<https://perma.cc/EZ4V-AN76>].

<sup>2</sup> Tae Kim, *Trump Hits the Fed Again in Tweet: ‘Tightening Now Hurts All That We Have Done’*, CNBC (July 20, 2018, 8:54 AM), <https://www.cnbc.com/2018/07/19/trump-lays-into-the-fed-says-hes-not-thrilled-about-interest-rate-.html> [<https://perma.cc/W8QC-9XU9>].

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> Jim Puzzanghera, *Trump Escalates His Criticism of Federal Reserve*, L.A. TIMES (July 20, 2018, 2:35 PM), <http://www.latimes.com/business/la-fi-trump-federal-reserve-20180720-story.html>.

Chairman Arthur Burns to maintain low interest rates in response to pressure from President Richard Nixon.<sup>6</sup>

The interest rate at issue is known as the “Federal Funds Target Rate” or simply the “fed funds rate.” This rate is important because it is a tool used by the Federal Reserve to influence monetary policy which in turn affects inflation, employment, and therefore the overall economy.<sup>7</sup> The fed funds rate represents the rate at which lending depository institutions loan surplus balances in their reserve accounts to borrowing institutions in need of raising liquidity overnight.<sup>8</sup> To raise the fed funds rate, the Fed sells government bonds which thereby decreases liquidity and raises rates because banks have less surplus funds to loan.<sup>9</sup> Conversely, in order to lower the fed funds rate, the Fed will buy government bonds, thereby increasing liquidity and thus the amount of funds available for banks to loan.<sup>10</sup> In general, low interest rates are used to stimulate and grow the economy, while raising rates are used to slow economic growth and inflation.<sup>11</sup> This occurs because when interest rates are low, the cost of borrowing money becomes cheaper.<sup>12</sup> When the cost of borrowing is inexpensive, firms and businesses are more willing to invest in expansion, leading to higher employment rates.<sup>13</sup> As a result of high employment, households become more willing to spend, causing a cycle that further

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<sup>6</sup> Will Martin & Bob Bryan, *Trump Just Attacked the Fed Again—an Ugly Economic Lesson from the Nixon Administration Shows Why His Criticism is so Worrying*, BUS. INSIDER (Aug. 21, 2018, 6:04 AM), <https://www.businessinsider.com/trump-federal-reserve-interest-rate-attacks-echo-nixon-disaster-2018-8> [<https://perma.cc/2J26-7UP2>] (attributing the economic period of stagflation in the 1970s to President Nixon’s pressure on Arthur Burns to keep interest rates low prior to the 1972 election).

<sup>7</sup> *How Does Monetary Policy Influence Inflation and Employment?*, BD. OF GOVERNORS OF THE FED. RESERVE SYS., [https://www.federalreserve.gov/faqs/money\\_12856.htm](https://www.federalreserve.gov/faqs/money_12856.htm) [<https://perma.cc/8G6C-3PLH>] (last updated Dec. 16, 2015).

<sup>8</sup> *Effective Federal Funds Rate [FEDFUNDS]*, FED. RESERVE BANK OF ST. LOUIS: FRED, <https://fred.stlouisfed.org/series/FEDFUNDS> [<https://perma.cc/2TBQ-QYBQ>] (last visited Sept. 7, 2018).

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> *How Does Monetary Policy Influence Inflation and Employment?*, *supra* note 7.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* (“[W]hen short- and long-term interest rates go down, it becomes cheaper to borrow.”).

stimulates the economy and encourages even more employment.<sup>14</sup> However, as the economy grows, so does the expectation that it will continue to do so, leading to higher inflation.<sup>15</sup> To reduce monetary expansion, the Fed undertakes a strategy known as “normalization” by lowering liquidity and thereby forcing interest rates higher.<sup>16</sup> Higher interest rates make it more expensive to borrow money, thus providing firms with less incentive to invest in growing their business.<sup>17</sup> The value of the U.S. dollar also rises with interest rates as foreign investors seek higher returns, but at the same time U.S. businesses see lower profitability abroad.<sup>18</sup> U.S. investors also fear a decrease in stock prices as the price an investor is willing to pay for a stock is determined by taking expected future earnings and discounting them (dividing) by current interest rates (the rate an investor could receive by buying low risk bonds).<sup>19</sup> Naturally, when dividing future earnings by a higher denominator the result of higher interest rates is thus lower stock prices.<sup>20</sup>

This paper will first undertake a brief history of the Fed’s independence in Section B, including a brief discussion on the constitutionality of the Fed, and a summary of the most recent instances of presidential pressure on the Chairman. In Section C I will discuss current legal challenges to independent government financial agencies before finally evaluating whether the Fed is truly independent of external political pressures in Section D.

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<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> Kate Stalter, *How Rising Interest Rates Affect Your Investments*, U.S. NEWS & WORLD REP. (Apr. 4, 2018, 9:30 AM), <https://money.usnews.com/money/blogs/the-smarter-mutual-fund-investor/articles/2018-04-04/how-rising-interest-rates-affect-your-investments> (explaining the impact of high interest rates on equity and fixed-income markets and the process of “normalization”).

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.* (“Simple math tells us that higher interest rates would make a company’s stock worth less today.”).

## B. Brief History

In 1913 President Woodrow Wilson signed the Federal Reserve Act, from which today's Federal Reserve System was born.<sup>21</sup> While the Fed is mandated by Congress to use monetary policy to maximize employment and stabilize economic growth, the Fed's most publically debated duty is to set the fed funds rate.<sup>22</sup> The fed funds rate is set by the Federal Open Market Committee (FOMC) which meet eight times a year to observe current economic trends and make monetary policy decisions based on their findings.<sup>23</sup> To do so, the FOMC takes note of a number of economic indicators including price and wage trends, employment levels, consumer spending, business investment levels, and foreign exchange rates.<sup>24</sup> The fed funds rate influences long-term lending rates such as mortgages, loans, and savings rates.<sup>25</sup> The FOMC is a committee of twelve members including the seven members of the Board of Governors of the Federal Reserve, the president of the Federal Reserve Bank of New York, and four rotating Reserve Bank presidents from the remaining eleven regional banks.<sup>26</sup>

### 1. Federal Reserve Independence

The Federal Reserve is an independent government agency accountable to the public and to Congress, and not directly to the President.<sup>27</sup> Congress mandates that maximum employment and

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<sup>21</sup> *What is the Purpose of the Federal Reserve System?*, BOARD GOVERNORS FED. RESERVE SYS., [https://www.federalreserve.gov/faqs/about\\_12594.htm](https://www.federalreserve.gov/faqs/about_12594.htm) [https://perma.cc/YZF5-ZCNR] (last updated Nov. 3, 2016).

<sup>22</sup> *How Does Monetary Policy Influence Inflation and Employment?*, *supra* note 11.

<sup>23</sup> *Effective Federal Funds Rate [FEDFUNDS]*, *supra* note 8.

<sup>24</sup> *Id.*

<sup>25</sup> *Id.* (“[T]he federal funds rate indirectly influences longer- term interest rates such as mortgages, loans, and savings, all of which are very important to consumer wealth and confidence.”).

<sup>26</sup> *Federal Open Market Committee: About the FOMC*, BOARD GOVERNORS FED. RESERVE SYS., [https://www.federalreserve.gov/faqs/about\\_12799.htm](https://www.federalreserve.gov/faqs/about_12799.htm) [https://perma.cc/YT8W-S5VD] (last updated Sept. 17, 2018).

<sup>27</sup> *What Does it Mean that the Federal Reserve is “Independent Within the Government”?*, BOARD GOVERNORS FED. RESERVE SYS., [https://www.federalreserve.gov/faqs/about\\_12799.htm](https://www.federalreserve.gov/faqs/about_12799.htm) [https://perma.cc/8WNQ-6Q3B] (last updated Mar. 1, 2017).

economic price stability are the two main macroeconomic goals of the Fed.<sup>28</sup> To ensure the Fed makes long-term decisions irrespective of politics, Congress strategically structured the Fed to maximize political insulation.<sup>29</sup> Elected officials, most notably the President, wish to see low interest rates and thus a growing economy as they seek approval and/or reelection.<sup>30</sup> Consequently, the long-term goal of controlling growth and inflation held by the Fed is often at odds with the President's goal of short-term growth that raises his chance of reelection.<sup>31</sup> To combat this disparity, the Fed is structured as an independent agency.<sup>32</sup> Members of the FOMC are appointed to fourteen-year terms, thus spanning multiple presidencies, while the Chairman and Vice Chairman of the Federal Reserve are appointed by the President to four year terms.<sup>33</sup> No elected official or member of the President's administration may serve on the Federal Reserve Board.<sup>34</sup> Furthermore, the Fed is not funded through the Congressional budgetary process, but rather the Fed's income primarily comes from interest on government securities and a number of other sources including interest on foreign currency investments, fees for services to depository institutions, and interest on loans to depository institutions.<sup>35</sup> Surplus earnings made by the Fed are turned over to the U.S. Department of the Treasury after paying the Fed's expenses.<sup>36</sup>

## 2. *Constitutionality of the Federal Reserve*

Since before the Fed's creation in 1913, strict constructionists argued whether the creation of a national bank was unconstitutional. The arguments for and against a national bank are captured in the

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<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> Jim Puzanghera & Don Lee, *Is the Fed Politically Biased? Look at its Interest-rate Decisions as Elections Near*, L.A. TIMES (Sept. 19, 2016, 5:00 AM), <http://www.latimes.com/business/la-fi-federal-reserve-election-2016-0919-snap-story.html>.

<sup>31</sup> *Id.* (detailing the internal struggles of the Fed during election cycles to appear independent of short-term political concerns).

<sup>32</sup> *What Does It Mean That the Federal Reserve Is "Independent Within the Government"?*, *supra* note 27.

<sup>33</sup> *Federal Open Market Committee: About the FOMC*, *supra* note 26.

<sup>34</sup> *What Does It Mean That the Federal Reserve Is "Independent Within the Government"?*, *supra* note 27.

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*



historic debate between Thomas Jefferson and Alexander Hamilton, in which Jefferson argued that Congress should not overstep its enumerated or elicited powers, while Hamilton argued that the creation of a national bank was within the Constitution's "implied powers" as Congress has the power to "coin money and regulate the Value thereof" while also possessing the power to adopt "all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers."<sup>37</sup> In *McCulloch v. Maryland* Chief Justice John Marshall settled the debate using much of Hamilton's reasoning to uphold the constitutionality of the Second Bank of the United States.<sup>38</sup> Today's Federal Reserve System is justified based on Hamilton's "implied powers" reasoning and thus any constitutional challenge to the Fed would require at least a partial overturn of *McCulloch*.<sup>39</sup>

Article II, Section 2, Clause 2 of the Constitution, the Appointments Clause, provides further debate on the constitutionality of the Fed's structure.<sup>40</sup> Under Article II, Section 2 the President has the power to appoint "Officers of the United States" with the Senate's advice and consent.<sup>41</sup> Congress also has the ability to vest power in "the President alone, in the Courts of Law, or in the Heads of Departments" the appointment of "inferior officers."<sup>42</sup> In *Edmonds v. United States*, the Supreme Court held that an inferior officer is one who has a superior appointment by the President and confirmed by the Senate.<sup>43</sup> It is clear that the Chairman is an officer of the United States as the individual chosen for the role is appointed by the President and

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<sup>37</sup> See U.S. Const. art. I, § 8, cl. 5, 18; Walker F. Todd, *Money and Banking: A Constitutional Perspective*, 35 CATO J. 193, 197–200 (2015) (detailing the historic debate over the first and second national banks between Jefferson and Hamilton).

<sup>38</sup> 17 U.S. 316 (1819); Todd, *supra* note 37 (observing similarities between Chief Justice Marshall's reasoning and the reasoning articulated by Hamilton in vouching for the National Bank).

<sup>39</sup> Todd, *supra* note 37 ("So if you do not like the Federal Reserve System, you have to figure a way either to persuade Congress to repeal or revise it, or to re-argue *McCulloch v. Maryland* and persuade the Supreme Court that Chief Justice Marshall was wrong.").

<sup>40</sup> See Peter Conti-Brown, *The Institutions of Federal Reserve Independence*, 32 YALE L.J. ON REG. 257, 293 (2015) (arguing that the structure of the Fed is not necessarily consistent with the Constitution's contemplated structure of an executive agency).

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> See 520 U.S. 651, 662–63 (1997).

confirmed by the senate; however, the Reserve Bank Presidents who sit on the FOMC appear to also be officers.<sup>44</sup> Although the process for appointing them does not conform to the requirements of the Appointment's Clause and the process for removing them violates the Supreme Court's decisions addressing the removal of officers.<sup>45</sup> The questionable constitutionality of the Federal Reserve highlights the attempt for true, politically insulated independence of the system.<sup>46</sup>

### 3. *Past Public Presidential Pressure on the Chairman*

The critical response to President Trump's comments on interest rates are in large part due to the fact they are the first time a President has publically commented on rates in decades.<sup>47</sup> While in the midst of a re-election campaign, then-President George H.W. Bush told the New York Times in 1992, "I'd like to see another lowering of interest rates. . . . I can understand people worrying about inflation. But I don't think that's the big problem now."<sup>48</sup> A week later, the Fed cut the Fed Funds Target by 0.5%, and by another 0.25% about a month prior to the election.<sup>49</sup> Despite the lowered rates, Bush insisted in a 1998 interview that he lost the re-election because then-Chairman Alan Greenspan did not lower rates enough after the 1990–91 recession, stating "I reappointed him, and he disappointed me."<sup>50</sup>

President H.W. Bush's harsh comments were not unprecedented. Two decades earlier President Nixon also pressured the Fed to lower rates in the midst of an eventually successful re-election bid.<sup>51</sup>

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<sup>44</sup> *Id.* (explaining how FOMC member Federal Reserve Presidents appear to be officers).

<sup>45</sup> Conti-Brown, *supra* note 40, at 293.

<sup>46</sup> *See id.* (arguing that "[t]he unconstitutionality of the Reserve Banks' governance highlights the way that law, politics, and custom interact to create a separate policy-making space for the Federal Reserve").

<sup>47</sup> Puzanghera, *supra* note 5.

<sup>48</sup> *Id.*

<sup>49</sup> *Id.*

<sup>50</sup> *Bush Pins the Blame for '92 Election Loss on Alan Greenspan*, WALL ST. J., Aug. 25, 1998, at A16 (quoting President Bush in an interview with David Frost stating, "I think that if the interest rates had been lowered more dramatically that I would have been re-elected president because the [economic] recovery that we were in would have been more visible.").

<sup>51</sup> Patrick Hosking, *Don't Mess with the Fed: A Lesson for Trump*, TIMES, Aug. 25, 2018, at 44, 45 (detailing President Nixon's pressure on Arthur Burns to cut interest rates to boost his re-election bid).

As unemployment slowly rose during Nixon's first term as president, Nixon pressured then-Chairman Arthur Burns telling him, "[y]ou can lead 'em. You always have, now. Just kick 'em in the rump a little."<sup>52</sup> In turn, the Fed lowered rates to 4.5% in 1972, which according to some economists ushered in a long period of inflation and higher unemployment.<sup>53</sup> This period of stagflation, marked by high inflation, high unemployment, and low economic growth, was not corrected until the Fed ratcheted up interest rates approximately a decade later in what is known as the "Volcker Shock," named for then-Chairman Paul Volcker.<sup>54</sup> However, not all economists agree that the 1970s interest rate cuts were to blame for the stagflation.<sup>55</sup> The mid-70s also saw the Yom Kippur War and Middle East oil embargo send oil prices soaring, which some insist explains the spike in US inflation.<sup>56</sup> While today's economy is markedly different from that of the 1970s, economists still warn that the lessons learned then still ring true, and that our central banking system should remain independent.<sup>57</sup>

### C. Current Legal Challenges to Independent Financial Policy

A potential circuit split on the constitutionality of an independent government financial bureau's structure could set the stage for a U.S. Supreme Court grant of certiorari.<sup>58</sup> The cases are focused on the constitutionality of the Consumer Financial Protection Bureau (CFPB), an independent agency established by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 that is funded by the Federal Reserve and led by a single Director who is appointed by the

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<sup>52</sup> *Id.*

<sup>53</sup> *Id.* (citing Burton Abrams, economics professor at the University of Delaware, who believes Burns actions to lower interest rates "helped to trigger an extremely costly inflationary boombust cycle" in the mid-70s).

<sup>54</sup> Martin & Bryan, *supra* note 6.

<sup>55</sup> Hosking, *supra* note 51 (citing a quote from Paul Ashworth, chief U.S. economist at Capital Economics, stating "Unless Arthur Burns secretly greenlighted the Yom Kippur War, you can't really blame him for the oil embargo and the quadrupling of oil prices in 1974. That explains most of the spike in US inflation.").

<sup>56</sup> *Id.*

<sup>57</sup> Martin & Bryan, *supra* note 6.

<sup>58</sup> Jeff Reynolds, *CFPB Lawsuits Could Create 'Circuit Split'*, HEARTLAND INST. (Aug. 13, 2018), <https://www.heartland.org/news-opinion/news/cfpb-lawsuits-could-create-circuit-split> [<https://perma.cc/TL5N-NV6K>].

President for a five year term but who can only be removed for cause.<sup>59</sup> The appointment of an independent director was meant to insulate the agency from pressure from Wall Street and other political lobbies.<sup>60</sup>

The CFPB faced a constitutional challenge in the D.C. Circuit in 2016.<sup>61</sup> Writing for a three-judge panel of the Court of Appeals for the District of Columbia, Judge Brett Kavanaugh struck down the structure of the CFPB on constitutional grounds.<sup>62</sup> Kavanaugh claimed the Director of the CFPB is the “single most powerful official in the entire United States Government, at least when measured in terms of unilateral power” other than the President.<sup>63</sup> In the opinion Kavanaugh also wrote, “[t]he concentration of massive, unchecked power in a single Director marks a dramatic departure from settled historical practice and makes the CFPB unique among traditional independent agencies . . . .”<sup>64</sup> However, in an *en banc* appeal the D.C. Circuit overturned Kavanaugh’s ruling and held the CFPB’s structure constitutional, citing *Humphrey’s Executor v. United States*, a 1935 case in which the Supreme Court found that for-cause removal was permissible as applied to the Federal Trade Commission commissioners.<sup>65</sup>

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<sup>59</sup> Daniel Bush, *What is the Consumer Financial Protection Bureau, Anyway?*, PBS NEWS HOUR (Nov. 27, 2017, 4:39 PM), <https://www.pbs.org/newshour/economy/making-sense/what-is-the-consumer-financial-protection-bureau-anyway> [<https://perma.cc/Y6J5-AH2X>].

<sup>60</sup> Jonnelle Marte, *This Court Case Could Have a Huge Impact on the Future of a Key Consumer Watchdog*, WASH. POST (May 24, 2017), [https://www.washingtonpost.com/news/get-there/wp/2017/05/23/federal-court-will-hear-arguments-on-whether-the-structure-of-cfpb-is-constitutional/?noredirect=on&utm\\_term=.589dbbc310a5](https://www.washingtonpost.com/news/get-there/wp/2017/05/23/federal-court-will-hear-arguments-on-whether-the-structure-of-cfpb-is-constitutional/?noredirect=on&utm_term=.589dbbc310a5).

<sup>61</sup> *PHH Corp. v. Consumer Fin. Prot. Bureau*, 839 F.3d 1 (D.C. Cir. 2016), *rev’d en banc*, 881 F.3d 75 (D.C. Cir. 2018).

<sup>62</sup> Tucker Higgins, *The Supreme Court Could Cripple an Obama-era Consumer Finance Watchdog if Agency Critic Brett Kavanaugh is Confirmed*, CNBC (July 10, 2018, 5:06 PM) <https://www.cnbc.com/2018/07/10/scotus-could-cripple-cfpb-with-brett-kavanaugh-on-the-bench.html> [<https://perma.cc/JTP9-J8G9>].

<sup>63</sup> 839 F.3d at 16.

<sup>64</sup> *Id.* at 17.

<sup>65</sup> *PHH Corp. v. Consumer Fin. Prot. Bureau*, 881 F.3d 75 (D.C. Cir. 2018) (*en banc*) (citing *Humphrey’s Ex’r v. United States*, 295 U.S. 602, 626 (1935)). See also Eric J. Mogilnicki & Ethan Levisohn, *PHH v. CFPB: The Impact on the Bureau’s Future*, NAT’L L. REV. (Feb. 2, 2018), <https://www.natlawreview.com/article/phh-v-cfpb-impact-bureau-s-future> [<https://perma.cc/EAU8-MXD9>].

In February 2017, the CFPB, alongside the New York Attorney General, filed a suit against RD Legal Funding LLC alleging fraud related to 9/11 victim compensation payments and payments to football players with brain injuries.<sup>66</sup> Judge Loretta Preska of the U.S. District for the Southern District of New York concluded that the structure of the CFPB was unconstitutional.<sup>67</sup> In her decision, Judge Preska disagreed with the D.C. circuit’s majority *en banc* decision and instead sided with the dissent in that case, stating that the CFPB is “unconstitutionally structured because it is an independent agency that exercises substantial executive power and is headed by a single director.”<sup>68</sup> This ruling comes while the Ninth and Fifth circuits have two similar constitutional challenges pending before them.<sup>69</sup> The inconsistent rulings and pending cases throughout the country have policy analysts predicting, and calling for, Supreme Court clarity surrounding the isolation of financial agencies.<sup>70</sup> On September 6, 2018 petitioners filed a petition for certiorari with the Supreme Court in the case *State National Bank of Big Spring v. Mnuchin*<sup>71</sup> which also seeks to argue the CFPB is unconstitutional on the grounds the CFPB violates the Constitution’s separation of powers provisions due to a lack of checks by the legislature, executive, and judicial branches.<sup>72</sup>

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<sup>66</sup> *Consumer Fin. Prot. Bureau v. RD Legal Funding, LLC*, 332 F. Supp. 3d 729 (S.D.N.Y. 2018).

<sup>67</sup> *Id.* at 784.

<sup>68</sup> *Id.* (quoting *PHH Corp. v. Consumer Fin. Prot. Bureau*, 881 F.3d 75 (D.C. Cir. 2018) (Kavanaugh, J., dissenting)); Vaishali Rao, Hinshaw & Culbertson LLP, *Is CFPB’s Constitutionality Headed for the U.S. Supreme Court?*, JDSUPRA (June 25, 2018) <https://www.jdsupra.com/legalnews/is-cfpb-s-constitutionality-headed-for-42690> [<https://perma.cc/JA3Z-9HSF>].

<sup>69</sup> Evan Weinberger, *N.Y. Judge Adds Fire to CFPB Constitutionality Question*, BLOOMBERG (June 22, 2018), <https://www.bna.com/ny-judge-adds-n73014476808>.

<sup>70</sup> Reynolds, *supra* note 58 (citing Daniel Press, a policy analyst for the Competitive Enterprise Institute, stating “You just cannot have a critical agency—something that is a very substantial part of the financial regulatory regime—being struck down as unconstitutional by different courts around the country. . . . That’s crazy. We’re going to need some clarity from the Supreme Court.”).

<sup>71</sup> *Petition for Writ of Certiorari, State Nat’l Bank of Big Spring v. Mnuchin* (No. 18-307), 2018 WL 4331933.

<sup>72</sup> *Supreme Court Asked to Hear Challenge to Constitutionality of Consumer Financial Protection Bureau*, COMPETITIVE ENTERPRISE INST. (Sept. 7, 2018), <https://cei.org/content/supreme-court-asked-hear-challenge-constitutionality-consumer-financial-protection-bureau> [<https://perma.cc/C3QC-L894>]

#### D. Is the Federal Reserve Truly Independent from Executive Pressure?

Despite the Fed's carefully chosen structure, it does not appear the system has achieved true political isolation.<sup>73</sup> Structurally, while Fed Board members are strategically appointed to fourteen-year terms, the members frequently retire before the end of their tenure, leading to more turnover than designed.<sup>74</sup> Further, the Chairman, appointed by the President, has a large amount of influence over the FOMC, as the Chairman holds final appointment powers within the Fed and sets meeting agenda.<sup>75</sup> Evidence from voting records, memorandum, and transcripts of FOMC meetings under Burns and Greenspan point to presidential influence on Fed priorities and FOMC voting.<sup>76</sup> Studies have found that Presidents tend to appoint Chairmen, Vice Chairmen, and Vice Chairmen for Supervision along party lines early in their presidencies, while late in their presidencies they tend to appoint members who appease special interest groups.<sup>77</sup> However, other studies indicate that regardless of appointments, monetary policy remains largely intact with the changing of presidential administration.<sup>78</sup> Administrations do, however, have the chance to influence monetary policy through traditional weekly meetings between the Chairman and the Administration designed to coordinate policy efforts.<sup>79</sup> Not unexpectedly, studies also show presidential appointees' voting patterns change preceding elections, which commenters believe suggests an "adjustment of Fed policy to promote the electoral success of their respective party."<sup>80</sup> Further, studies even show that monetary policy in election years tends to be stimulative, returning to restrictive in years succeeding elections.<sup>81</sup>

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(announcing a petition for certiorari filed with the Supreme Court challenging the CFPB's structure).

<sup>73</sup> Peter J. Boettke & Daniel J. Smith, *Federal Reserve Independence: A Centennial Review*, 1.1 J. PRICES & MKTS. 31, 31–48 (2013).

<sup>74</sup> *Id.* at 33.

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

### **E. Conclusion**

While President Trump's recent public sentiments regarding the Fed were shocking to some political and economic pundits, they were not unprecedented (aside from the use of the chosen medium). Evidence shows that presidential administrations have influenced monetary policy in the past through both public and back channels. However, President Trump should take note of President Nixon's mistakes and tread lightly, as pressuring the Fed runs the risk of ushering in a long period of stagflation long past the end of his presidency.

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